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By E-mail

27 June 2008

Clerk to the Public Works Subcommittee
Legislative Council Building
8 Jackson Road
Central, Hong Kong
(Attn: Ms Angel Shek)

Dear Ms Shek,

**Public Works Subcommittee
Follow-up to meeting on 18 June 2008**

Item PWSC(2008-09)31

**21QJ – An upfront endowment to the West Kowloon Cultural District
Authority for developing the West Kowloon Cultural District**

I refer to your letter dated 20 June 2008 enclosing a list of issues requiring follow-up actions by the Administration. Please find attached the bilingual reply.

Yours sincerely,

(Howard LAM)
for Secretary for Home Affairs

Encl.

c.c. Secretary for Financial Services and the Treasury
(Attn: Mr Jack Chan)

**Public Works Subcommittee
Meeting on 18 June 2008**

Item PWSC(2008-09)31

21QJ – An upfront endowment to the West Kowloon Cultural District Authority for developing the West Kowloon Cultural District

Administration's response to the list of issues requiring follow-up actions by the Administration before the relevant meeting of the Finance Committee

Q.1 In relation to members' concern that the provision of a one-off upfront endowment to the West Kowloon Cultural District Authority (WKCDA) might deprive the Legislative Council (LegCo) of a proper oversight in the disposal of public resources during the development and management of WKCD, the Administration was requested to consider putting in place measures to hold WKCDA accountable to the public for the fund spent, having regard to the request of Hon Alan LEONG for regular reports on a half-yearly basis to provide information including but not limiting to the following:

- (a) Staff establishment;**
- (b) Estimates and actual expenditure for staff remuneration and other personnel-related expenses;**
- (c) Estimates and actual expenditure for outsourcing services;**
- (d) Detailed plans on the delivery of various construction projects for the development of WKCD;**
- (e) Estimates and actual expenditure for each construction project with breakdown by expenditure items;**
- (f) Progress and delay in the delivery of the construction projects;**
- (g) Business plans for the Core Arts and Cultural Facilities;**
- (h) Business plans for the retail/dining/entertainment (RDE) at the commercial sites in WKCD;**
- (i) Other information requested by the LegCo and its relevant committees.**

A.1 The WKCDA Bill, together with our proposed Committee Stage Amendments to the Bill include a series of provisions to enhance the corporate governance and financial management of the Authority. The relevant measures are as follows –

Corporate Governance

The Bill provides that the WKCDA shall prepare and submit an annual report to the Financial Secretary. The report must specify the work and

activities of the Authority for that financial year and how they relate to the Authority's functions and objectives, the work and activities of the committees, the statement of accounts and the auditor's report. The report shall be laid on the table of the LegCo.

The Bill also requires that the WKCD A has to submit a corporate plan covering a programme of activities and projects that the Authority plans to conduct for the next three years, and a business plan covering the details of the activities and projects that are to be conducted or implemented in the next financial year to the Secretary for Home Affairs for record purpose.

Audit Arrangements

The Bill requires the WKCD A to set up an Audit Committee. To tally with the practices of listed companies, the Bill will also require that the Audit Committee of the Authority shall consist of at least one member who possesses appropriate qualifications or expertise in accounting or financial management.

In addition, the Director of Audit may conduct an examination into the economy, efficiency and effectiveness with which the WKCD A has expended its resources in performing its functions.

Enhancing public accountability

The WKCD A Bill requires the Chairman and the Chief Executive Officer of the WKCD A to attend meetings of the LegCo upon request, and answer questions raised by LegCo Members.

Avoiding Conflict of Interest

The Bill provides that a board member or committee member will have to disclose any interest that he has upon his first appointment and also at the beginning of every year after the appointment. A member also has to disclose his interest if he becomes aware of any interest not previously disclosed, or if there is change to the interest disclosed.

The WKCD A, its committees and any body corporate established by it will be included in Schedule One of the Prevention of Bribery Ordinance such that their members will be subject to the relevant provisions of the Ordinance. The Bill also includes WKCD A into Schedule 1 of the Ombudsman Ordinance such that it will be subject to the Ombudsman's scrutiny.

Financial Management

The Bill provides that the WKCDA shall manage its finances with due care and diligence, and shall invest in a financially prudent manner, in such classes or descriptions of investment as specified by the Financial Secretary.

The Bill also requires that the WKCDA should establish an Investment Committee for the purposes of monitoring investments made by the WKCDA and overseeing the management of such investments. The committee chairman and members should possess expertise or experience in the fields related to the duties of the committee.

Reporting to LegCo on use of the upfront endowment

We plan to put in place the following arrangements for reporting to LegCo on the use of the upfront endowment by WKCDA:

- (a) Under the Bill, the WKCDA shall submit to the Financial Secretary, within six months after the end of each financial year, an Annual Report for each financial year which contains an audited statement of accounts prepared in accordance with the relevant provisions in the Bill and related information. The Financial Secretary shall cause the Report to be laid on the table of LegCo. The submission of the financial information in Annual Reports is effectively a yearly reporting procedure on the use of finances by the WKCDA in LegCo. In addition to this annual reporting, we would be reporting to LegCo as and when we see there is a need to do so.
- (b) We would request the WKCDA to conduct a mid-term review after the completion of the core arts and cultural facilities in Phase I or not later than 2014-15, on the progress of the Phase I facilities as well as its plan for developing the Phase II facilities. The WKCDA has to report on the results of this review to LegCo or any relevant committee of LegCo.
- (c) The Bill provides that the LegCo or any relevant committee of the LegCo may request the Chairman and the Chief Executive Officer of the WKCDA to attend its meetings and answer questions, including questions on financial information in its Annual Reports after they have been tabled in the LegCo. We believe that the WKCDA would also make good use of attending meetings in LegCo to report on, and collate views on major matters relating to its functions from time to time.

We consider the proposal to require half-yearly reports on a host of matters relating not only to the use of financial resources by WKCDA, but also business, operation and management of the WKCDA, may not be conducive to effective reporting and monitoring of the use of the upfront endowment by WKCDA, while providing adequate flexibility for the WKCDA to carry out its functions.

Taking into account the above, we consider we have in place sufficient public accountability and control measures to ensure that WKCDA will be accountable to the public for the use of public resources.

Q.2 At the request of Hon LEE Wing-tat, the Administration was requested to provide information on whether an interim review of the financial arrangements would be conducted following the completion of Phase I development of the WKCD project in around 2013-2014, and if so, whether and how the results would be reported to LegCo.

A.2 We would request the WKCDA to conduct a mid-term review after the completion of the core arts and cultural facilities¹ in Phase I or not later than 2014-15, on the progress of the Phase I facilities as well as its plan for developing the Phase II facilities. The WKCDA has to report on the results of this review to LegCo or any relevant committee of LegCo.

In reporting on the results of this mid-term review the WKCDA has to provide the following information –

- (1) the overall progress of the development of the Phase I facilities, including completed and unfinished facilities (if any);
- (2) the capital costs of developing the Phase I facilities;
- (3) the overall financial position and operating results of the WKCD project, including the audited income and expenditure accounts; and
- (4) the initial forecast and planning for, as well as initial financial estimates of the Phase II facilities.

Q.3 In relation to the concerns of Hon Abraham SHEK and Dr Hon KWOK Ka-ki that the 119 000 square metres of land provided for RDE facilities to generate rental income to subsidize operating

¹ The core arts and cultural facilities in Phase I cover a Mega Performance Venue, a Great Theatre, two Medium-sized Theatres, four Blackbox Theatres, a Concert Hall, a Chamber Music Hall, a Xiqu Centre (including a large and a small theatre), Piazza Areas, the M+ (Phase I) and an Exhibition Centre.

deficits of the arts and cultural facilities should be taken into account as part of the public resources allocated for the WKCD project, the Administration was requested to provide, as far as practicable, the estimated premium for the relevant part of the land.

- A.3 The proposed financing arrangement is that retail/dining/entertainment (RDE) facilities will be vested with the WKCDA to provide a steady source of recurrent income through rental proceeds to meet the operating deficits. The vesting of RDE facilities with WKCDA seeks to enable the WKCD to be developed and operated as an integrated arts and cultural district in a financially sustainable manner without having to provide WKCDA with recurrent funding to cover its operating deficits on a long-term basis.

Under our proposed financial arrangement, as we have no intention to sell the RDE sites in the market, the question of land premium does not arise. According to the information contained in Annex 9 of the Financial Matters Advisory Group Report, the estimated land revenue for the RDE sites at a total GFA of 119,000 square metres is about \$3.2 billion (in 2006 net present value (NPV)).

- Q.4 To address the concern of Prof Hon Patrick LAU and Hon Emily LAU about the procurement approaches to be adopted for the development of WKCD, the Administration was requested to provide information on considerations given to different procurement approaches for the various facilities, including design and build approach, and the approach which would include design competition(s).**

- A.4 The WKCDA may consider the pros and cons of different modes of Public Private Partnership (PPP) in the development of the arts and cultural facilities with reference to the facilities' distinctive features. The Consultative Committee on the Core Arts and Cultural Facilities of the WKCD recommended that architectural design competition should be held for the M+, Xiqu Centre and Concert Hall/Chamber Music Hall. The WKCDA will take this recommendation into account in deciding on the organization of design competitions for the arts and cultural facilities.

- Q.5 To address Hon Emily LAU's concerns, the Administration was requested to:**

- (a) **Clarify and confirm whether there were past cases where similar funding approach had been adopted under which a statutory public body was granted with an upfront endowment by the Finance Committee to plan and implement infrastructure/capital works**

projects under its purview, and if so, information on the precedent cases. Please also explain how the funding approach for the WKCD project compares with that for other major infrastructure projects such as railway projects.

A.5(a) While we are not aware of any past cases where a statutory public body has been granted with an upfront endowment through a one-off funding approval by the Finance Committee (FC) to plan and implement infrastructure/capital works projects under its purview, the FC has approved one-off lump-sum injection or loans to statutory public bodies/statutory corporations/relevant funds to implement specific programmes/schemes. Such examples include equity injection into the Kowloon-Canton Railway Corporation (KCRC), Urban Renewal Authority (URA) and grants to various trust funds such as the Language Fund, Environmental and Conservation Fund, etc. For other major infrastructure projects, the funding approaches varied. Infrastructure facilities are normally funded on a project by project basis under our existing funding arrangement.

(b) Explain whether the future operation of the RDE facilities at WKCD, given the advantage of government investment in the capital costs, would run into direct and unfair competition to and pose adverse impact on other existing private RDE facilities in the vicinity.

A.5(b) According to the recommendations of the Performing Arts and Tourism Advisory Group (PATAG) under the Consultative Committee, retail facilities should spread over the district to achieve the synergy and clustering effect in an integrated arts and cultural district. As such, the retailing mix should reflect the character of the district as the cultural hub of Hong Kong. The WKCDA would take into account these factors in preparing the (master) development plan for the WKCD and planning for RDE facilities. Under the WKCDA Bill, the WKCDA has the responsibility to ensure the financial sustainability of the operation and management of arts and cultural facilities and other related facilities. As most of the arts and cultural facilities are loss-making, the RDE rental income received by the WKCDA will have to be ploughed back to sustain the operation of the arts and cultural facilities. Unlike the operators of any existing retail facilities in the commercial market, the WKCDA will have to bear the operating risk of the arts and cultural facilities, in addition to that of the RDE facilities

(c) Advise whether the net total rental income in excess of the estimated annual net total rental income of \$8.4 billion over the project period to 2059, if any, would be allocated to the WKCDA for the operation

and development of WKCD. Please also advise whether the WKCDA would set up a fund to manage the RDE income and surplus for the purpose of funding major repairs of facilities and human resources training (a request made by Hon Emily LAU after the PWSC meeting held on 18 June 2008).

A.5(c) The WKCDA Bill provides that the resources of the WKCDA consist of, among others, income received by the Authority by operating, managing or otherwise dealing with arts and cultural facilities, related facilities (including RDE) or ancillary facilities. Any excess of net total rental income from RDE over the net total operating deficits of CACF will therefore be the resources of the WKCDA for the operation and development of the WKCD.

Provisions (about \$2.9 billion in 2008 NPV) have been made in the one-off upfront endowment of \$21.6 billion (in 2008 NPV) to cover periodic major repairs and renovation of various arts and cultural facilities and other related facilities of WKCD so that all facilities are kept in good condition and fully functional during and beyond the 50-year project period.

The WKCDA Bill provides that the WKCDA shall perform its functions in ways which aim to achieve a number of arts and cultural development objectives. Training of human resources in the arts have been embedded in a number of these objectives, such as “to develop new and experimental works in arts and culture”, and “to cultivate and nurture local talents in the arts (including local artists), and local arts groups and arts-related personnel”.

**Home Affairs Bureau
June 2008**